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# CREDIT ISSUES

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## WOODGATE & CO.

Chartered Accountant  
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### RETENTION OF TITLE AND SECURITY INTERESTS

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#### Background

A retention of title clause is a term in a creditor's contract for the supply of goods which provides the creditor with protection against non-payment. It does this by stating that title to the goods does not pass until payment is received in full. It allows the creditor to recover goods, which it can then re-sell. However, to be commercially effective, the goods should be capable of resale to a third party.

A simple retention of title clause allows the creditor to recover only those goods which are unpaid on a specific invoice basis, potentially creating problems of identification and accounting. The more complex all-monies retention of title clause solves those problems, by allowing the creditor to recover any goods it has supplied, even if the goods located at the debtor's premises have been paid for by the debtor.

Retention of title clauses are sometimes known as Romalpa clauses, so named after 1976 England and Wales Court of Appeal decision of Aluminium Industrie Vasseen B.V. v Romalpa Aluminium Ltd, which first established their effectiveness.

#### The Associated Alloys decision

A charge is a security arrangement which enables a lender to take possession of and realise property that it does not own. The *Corporations Act* pursuant to Section 262 requires charges to be registered. If a charge is not registered, it is at risk of being void, if a Voluntary Administrator or Liquidator is subsequently appointed to the debtor company.

The issue of whether a retention of title clause is a charge which must be registered with Australian Securities and Investments Commission was considered by the High Court of Australia in *Associated Alloys Pty Ltd v ACN 001 452 106 Pty Ltd (in liquidation)* ("Associated Alloys"). The Court found a clear distinction between a retention of title clause by which a creditor retains title, on the one hand, and a charge by which a lender obtains rights to property to which it never held legal title, on the other. The Court held that a retention of title clause was not a charge.

After the *Associated Alloys* case, the position regarding retention of title clauses was apparently clear. A retention of title clause would not

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require registration as a charge and would be effective, so long as it was effectively drafted and appropriately incorporated into the contract for the sale of goods.

### **What about registration under the *Victorian Chattel Securities Act* or equivalent legislation?**

However, a chain of litigation commencing in 2003 and culminating in a High Court of Australia decision earlier this year raised a further complexity. Even though registration as a charge with ASIC was not required by the *Corporations Act*, did the *Victorian Chattel Securities Act (Vic) 1987* require separate registration on the register maintained by the Roads Corporation of Victoria?

Section 3 of the *Chattel Securities Act* defines a security interest as:

*“an interest in or a power over goods...which secures payment of a debt or other pecuniary obligation or the performance of any other obligation and includes any interest in or power over goods of a lessor, owner or other supplier of goods.”*

Sub-section 3(3) provides:

*“a hirer or lessee of goods or a buyer of goods under a conditional sale is deemed to have an interest in the goods notwithstanding that title or general property in the goods has not passed to the hirer, lessee or buyer”.*

Section 7 of the *Chattel Securities Act* operates to extinguish an unregistered security interest, if there is a sale to a person who buys the goods, in good faith and without notice of the security interest. There is a similar provision in Section 9 of the *Registration of Interests in Goods Act 1986 (NSW)*.

### **General Motors Acceptance Corp Australia v Southbank Traders Pty Ltd**

Southbank Traders Pty Ltd (“Southbank”) was a motor vehicle wholesaler which sold ten motor vehicles to Kingstrate Pty Ltd (“Kingstrate”), a car dealership. The contract for sale of the motor vehicles included an all monies retention of title clause.

After taking possession of the vehicles Kingstrate sold one vehicle to a member of the public and another nine to a financier, General Motors Acceptance Corporation Australia LLC (“GMAC”), without paying the purchase price, as part of a floor plan financing arrangement. Floor plan finance is a type of finance found predominantly in the motor vehicle industry which allows the borrower to display vehicles and offer them for sale to the public.

GMAC registered its security interest under the *Chattel Securities Act*. However, Southbank had not registered its security interest under that Act.

Southbank sued GMAC for conversion of the nine vehicles. GMAC argued that the retention of title clause created a security interest which required registration under the *Chattel Securities Act* and that because of the failure to register, Southbank’s security interest was extinguished. Southbank argued that a retention of title clause did not operate to create a security interest in the goods. At first instance the County Court of Victoria accepted GMAC’s argument and held that the retention of title clause was a security interest, which had been extinguished by the failure to register the security interest.

Southbank appealed to the Court of Appeal of the Supreme Court of Victoria, which held that a retention of title clause was not a security interest as defined by the *Chattel Securities Act* and therefore did not require registration.

GMAC then appealed to the High Court. The High Court held that the definition of security interest under the *Chattel Securities Act* had clearly been intended to include conditional sales, such as retention of title arrangements. Southbank had failed to register its security interest and hence, lost the benefit of its security interest.

### **The bigger picture**

The High Court's decision was determined on the specific statutory meaning of security interest, as defined by the *Chattel Securities Act*. Pursuant to Section 13, the *Chattel Securities Act* only applies to motor vehicles, trailers, boats of less than 20m in length and agricultural equipment, which are situated in Victoria. The equivalent legislation in New South Wales is the *Registration of Interests in Goods Act*, which only requires the registration of security interests in motor vehicles and boats.

If a resident of New South Wales buys a motor vehicle from a resident of New South Wales and then relocates the equipment to Victoria in circumstances such that the motor vehicle should be registered in Victoria, then the *Chattel Securities Act* arguably applies, notwithstanding that contract was entered into outside of the jurisdiction.

Businesses that provide goods of the type to which the *Chattel Securities Act*, or the equivalent state legislation, applies and use a retention of title clause need to be aware that their clause may be ineffective, unless it is registered.

The case, when considered in light of the inconsistencies between state legislation, shows the need for the reform of personal property securities law. According to a discussion paper released by the standing committee of the Commonwealth and State Attorney-Generals in November 2006, there were over 70 different acts governing the law of personal property securities such as motor vehicles, boats and agricultural machinery. In April 2007 the Commonwealth Attorney General announced an in principle agreement with the States and Territories to create a single national register for loans secured by personal property. In May 2007 the Commonwealth Treasurer announced, in the budget, funding of \$113.3M for the new national register.

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